

Annex 4

Draft marked-up version of the Statutory Notification: USP accounting condition

This marked-up version of the Statutory Notification: USP accounting condition is provided as an aid to understanding but is not the legal instrument making the modification.

- Deletions are marked in red and struck-through text
- Additions are marked in red.

NOTIFICATION OF DECISION TO IMPOSE A REGULATORY CONDITION IN ACCORDANCE WITH SECTION 53 OF, AND PARAGRAPH 3(1) OF SCHEDULE 6 TO, THE POSTAL SERVICES ACT 2011

BACKGROUND

- (A) On 13 December 2011, at Annex 13 to the consultation document entitled '*Review of Regulatory Conditions: Postal Regulation*', OFCOM published a notification in accordance with section 53 of, and paragraph 3(3) of Schedule 6 to, the Act setting out their proposals to impose on Royal Mail a USP accounting condition pursuant to their powers in section 39 of the Act (the "**First Notification**").
- (B) A copy of the First Notification was sent to the Secretary of State in accordance with Schedule 6 paragraph 5(1)(a) of the Act.
- (C) In the First Notification (and the accompanying consultation document), OFCOM invited representations about any of the proposals set out therein by 31 January 2012.
- (D) By virtue of section 53 of, and paragraph 3(5) of Schedule 6 to, the Act OFCOM may give effect, with or without modifications, to a proposal with respect to which they have published a notification only if they—
- (i) have considered every representation about the proposal that is made to them within the period specified in the First Notification; and
 - (ii) have had regard to every international obligation of the United Kingdom (if any) which has been notified to them for this purpose by the Secretary of State.
- (E) OFCOM received responses to the First Notification and have considered every such representation made to them in respect of the proposals set out in the First Notification (and the accompanying consultation document); and the Secretary of State has not notified OFCOM of any international obligation of the United Kingdom for this purpose.

DECISION

1. OFCOM hereby impose, in accordance with section 53 of, and paragraph 3(1) of Schedule 6 to, the Act and pursuant to powers in section 39 of the Act, on Royal Mail a USP accounting condition to make provision for matters set out in that section 39, such as accounting separation, rules about the identification of costs etc.
2. The USP accounting condition imposed by OFCOM is set out in the Schedule hereto.
3. The effect of, and OFCOM's reasons for making, this decision are set out in the accompanying explanatory statement.

OFCOM'S DUTIES AND LEGAL TESTS

4. OFCOM are satisfied that this decision satisfies the general test in paragraph 1 of Schedule 6 to the Act.
5. In making this decision, OFCOM have considered and acted in accordance with their principal duty in section 29 of the Act and their general duties in section 3 of the Communications Act 2003.

INTERPRETATION

6. Except insofar as the context otherwise requires, words or expressions shall have the meaning assigned to them in this Notification and otherwise any word or expression shall have the same meaning as it has been ascribed for the purpose of Part 3 of the Act.
7. In this Notification—
 - (a) “**Act**” means the Postal Services Act 2011 (c.5);
 - (b) “**First Notification**” has the meaning given to it in recital (A) above; and
 - (c) “**Royal Mail**” means Royal Mail Group Ltd, whose registered company number in England and Wales is 04138203.
8. For the purpose of interpreting this Notification—
 - (a) headings and titles shall be disregarded;
 - (b) expressions cognate with those referred to in this Notification shall be construed accordingly;
 - (c) the Interpretation Act 1978 (c. 30) shall apply as if this Notification were an Act of Parliament.
9. The Schedule to this Notification shall form part of this Notification.
10. Unless otherwise is stated in that Schedule, this Notification shall take effect on 1 April 2012.

SCHEDULE

USP ACCOUNTING CONDITION

1.1. Application, definitions and interpretation

<p>USPAC</p> <p>1.1.1</p> <p><i>Application</i></p>	<p>This USP accounting condition ("USPAC Condition") shall apply to the <u>universal service provider</u>.</p>
<p>USPAC</p> <p>1.1.2</p> <p><i>Definitions</i></p>	<p>In this USPAC Condition—</p> <p>(a) "Access" has the meaning given to it for the purpose of section 38 of the <u>Act</u> and, in relation to giving a person access to <u>Royal Mail's postal network</u>, includes giving a person an entitlement to use, be provided with or become a party to any services, facilities or arrangements comprised in the <u>postal network</u>;</p> <p>(b) "Accounting Methodology Manual" means the document from time to time containing all the <u>Regulatory Accounting Methodology</u> used by <u>Royal Mail</u> to comply with obligations imposed by or under this USPAC Condition, in particular the requirements in the <u>Regulatory Accounting Guidelines</u>, except for the <u>National Costing Methodology</u> and the <u>Zonal Costing Methodology</u> which are both documented in the <u>Costing Manual</u>;</p> <p>(c) "Act" means the Postal Services Act 2011 (c.5);</p> <p>(d) "Annual Budget" means a document containing <u>Royal Mail's</u> budget for any <u>Financial Year</u>, including estimates of revenue, operating expenditure and capital expenditure for the <u>Financial Year</u> in question, relating to the activities undertaken by the <u>Relevant Group</u>;</p> <p>(e) "consolidated" means the combination of the accounts of persons corporate and unincorporate that make up the <u>Relevant Group</u>, applying the same methodologies used for consolidating the consolidated accounts of <u>RMH plc</u> encompassing any of its subsidiaries or holding companies, or any subsidiary of such holding companies (all as defined by section 1159 of the Companies Act 2006), or any group undertaking (as defined by section 1161 of the Companies Act 2006);</p> <p>(f) "Costing Manual" means the document from time to time containing <u>Royal Mail's</u> detailed description of the <u>National Costing Methodology</u> and the <u>Zonal Costing Methodology</u> and identifying all sources of data, and all supporting empirical data used for assumptions, used in the <u>National Costing Methodology</u> and the <u>Zonal Costing Methodology</u>;</p> <p>(g) "Financial Month" means each month comprised in the <u>Financial Year</u>;</p> <p>(h) "Financial Quarter" means each period of three consecutive</p>

months comprised in the Financial Year, the first quarterly period of which begins with the first month of the Financial Year;

(i) “**Financial Year**” means any period of twelve consecutive months for which the annual statutory financial statements of RMH plc are prepared, the first twelve month period of which begins on 26 March 2012;

(j) “**Four FREs**” has the meaning given to it in USPAC 1.5.1;

(k) “**Guiding Principles**” has the meaning given to it in USPAC 1.7.2;

(l) “**Inward Mail Centre**” means the part of the mail centre in which the activities relating to the processes of final sorting for delivery (in that mail centre’s catchment area) of mail received from the upstream part of the Royal Mail’s network, or from other postal operators, to the final addresses take place. The upstream part of Royal Mail’s network consists of the processes related to collection and distribution of mail;

(m) “**National Costing Methodology**” means the rules, procedures, methods, algorithms, assumptions and other processes used by Royal Mail for the purpose of assigning the costs of the Reported Business, which it incurs in the conduct of its business, without geographic differentiation in the United Kingdom to the products it provides in the course of that business, wherever those rules, procedures, methods, algorithms, assumptions and other processes may be set out;

(n) “**non-Mails**” means all of the products and/or services provided by the Reported Business that do not fall within the meaning of postal services, which products and/or services OFCOM may direct from time to time (in the Regulatory Accounting Guidelines or otherwise) to be treated as ‘non-Mails’ for the purpose of matters relating to this USPAC Condition;

(o) “**non-USO**” means all of the products and/or services provided by the Reported Business that are not part of USO products and/or services;

(p) “**PAF**” means ‘Postal Address File’, a database of all valid postal addresses and their postcodes in the United Kingdom, and the services provided by Royal Mail in relation to that database;

(q) “**POL**” means Post Office Limited, whose registered company number in England and Wales is 02154540, and any of its subsidiaries (as defined by section 1159 of the Companies Act 2006) or any of its subsidiary undertakings (as defined by section 1162 of the Companies Act 2006 and for which section Post Office Limited shall be treated as the parent undertaking);

(r) “**Qualified Independent Auditor**” means a person who is eligible for appointment as a statutory auditor under Part 42 of the Companies Act 2006 and, if the appointment were an appointment as a statutory auditor, would not be prohibited from acting by section 1214 of that Act (independence requirement);

(s) “Regulatory Accounting Guidelines” means the document so entitled and published by OFCOM (as amended from time to time) setting out such requirements as OFCOM may direct from time to time relating to the preparation, auditing, reporting and publication, of regulatory financial statements and other regulatory financial reports to be prepared and maintained by Royal Mail by or under this USPAC Condition;

(t) “Regulatory Accounting Methodology” means the rules, policies, procedures, methods, models (including tables, matrices, mappings, lists of accounts, codes and cost structures), calculations, algorithms, concepts, assumptions (including a description of any evidence underlying such assumptions) and any other processes, used by Royal Mail for the purpose of preparing regulatory financial statements and other regulatory financial reports;

(u) “Relay” means ‘Royal Mail Relay’, a contract-only service that provides a scheduled collection and delivery of urgent, or time-sensitive items to and from an agreed set of locations;

(v) “Relevant Group” means Royal Mail, and all persons corporate and unincorporate included in the statutory consolidated accounts of RMH plc, excluding RMH plc itself and POL;

(w) “Reported Business” means the part of Royal Mail’s business that undertakes activities for the purpose of, or in connection with, the provision of USO and non-USO (including, but not limited to, non-Mails), the fully allocated costs of which are derived by the National Costing Methodology and Zonal Costing Methodology as described in the Costing Manual. For the avoidance of doubt, those activities shall be treated to include all the activities, products and/or services which fall within the scope of the Costing Manual from time to time. The reference to fully allocated costs is a reference to a costing methodology in which all costs are allocated to the outputs of the business.

(x) “RMH plc” means Royal Mail Holdings plc, whose registered company number in England and Wales is 04074919;

(y) “Royal Mail” means Royal Mail Group Limited, whose registered company number in England and Wales is 04138203;

(z) “Strategic Business Plan” means Royal Mail’s business plan setting out its performance and vision for the activities undertaken by the Relevant Group including a forecast of revenue, operating expenditure, capital expenditure, expectations of change in the postal market, details of future planned initiatives (e.g. projects to improve efficiency) and Royal Mail’s view on appropriate quality of service targets;

(aa) “USO” means products and/or services provided by Royal Mail for the purpose of complying with its universal service obligations imposed by any designated USP condition; and

(bb) “Zonal Costing Methodology” means the rules, procedures,

	methods, algorithms, assumptions and other processes used by <u>Royal Mail</u> for the purpose of assigning the costs of the <u>Reported Business</u> , which it incurs in the conduct of its business, to the products for which it sets geographically differentiated prices, wherever those rules, procedures, methods, algorithms, assumptions and other processes identify cost differentials between specific zones defined by <u>Royal Mail</u> in accordance with its obligations by or under this USPAC Condition.
USPAC 1.1.3 <i>Interpretation</i>	<p>For the purpose of interpreting this USPAC Condition—</p> <p>(a) except in so far as USPAC 1.1.2 or the context otherwise requires, any word or expression shall have the same meaning as it has been ascribed for the purpose of Part 3 of the <u>Act</u>;</p> <p>(b) headings and titles shall be disregarded;</p> <p>(c) expressions cognate with those referred to in this USPAC Condition shall be construed accordingly;</p> <p>(d) the Interpretation Act 1978 (c. 30) shall apply as if this USPAC Condition were an Act of Parliament;</p> <p>(e) references to a “day” are references to a period of twenty-four hours beginning with one midnight and ending with the next, which period shall be treated to include a Saturday, a Sunday, a Bank Holiday, Christmas Day, Good Friday or other public holiday.</p>

1.2. General obligations

USPAC 1.2.1 <i>Consents etc.</i>	<p><u>Royal Mail</u> must act in the manner and form required by the obligations imposed by or under this USPAC Condition, except in so far as <u>OFCOM</u> may otherwise consent, approve or recommend in writing from time to time.</p>
USPAC 1.2.2 <i>Directions</i>	<p><u>OFCOM</u> may from time to time give such directions as they consider appropriate in relation to <u>Royal Mail</u>—</p> <p>(a) maintaining a separation for accounting purposes between such different matters as <u>OFCOM</u> may direct for such purposes as they may direct, including separation in relation to different services, facilities or products or in relation to services, facilities or products provided in different areas as well as the accounting methods to be used in maintaining the separation;</p> <p>(b) complying with rules made by <u>OFCOM</u> in relation to those matters about the identification of costs and cost orientation, including the application of presumptions in the fixing and determination of costs and charges for any purpose as well as the publication of such accounts and other information relating to anything required to be done by <u>OFCOM</u> in</p>

	<p>this regard;</p> <p>(c) complying with rules made by <u>OFCOM</u> about the use of cost accounting systems in relation to those matters, including the application of presumptions in the fixing and determination of costs and charges for any purpose as well as the publication of such accounts and other information relating to anything required to be done by <u>OFCOM</u> in this regard;</p> <p>(d) securing that <u>Royal Mail</u>'s compliance with those systems is audited annually by a <u>Qualified Independent Auditor</u>, including <u>Royal Mail</u> meeting the costs of the audit; and</p> <p>(e) otherwise in relation to <u>Royal Mail</u>'s obligations under this USPAC Condition.</p>
<p>USPAC</p> <p>1.2.3</p> <p><i>Compliance with directions</i></p>	<p><u>Royal Mail</u> must comply with any direction given by <u>OFCOM</u> from time to time under this USPAC Condition.</p>
<p>USPAC</p> <p>1.2.4</p> <p><i>Records retention</i></p>	<p>Except in so far as <u>OFCOM</u> may otherwise consent in writing from time to time, <u>Royal Mail</u> must keep for a period of six years all the financial statements and information required by or under this USPAC Condition.</p>

1.3. Obligations relating to the Relevant Group

<p>USPAC</p> <p>1.3.1</p> <p><i>Financial statements and information</i></p>	<p><u>Royal Mail</u> must prepare and maintain the following—</p> <p>(a) for each <u>Financial Year</u>, a <u>consolidated</u> income statement for the <u>Relevant Group</u>;</p> <p>(b) for each <u>Financial Year</u>, a <u>consolidated</u> balance sheet statement for the <u>Relevant Group</u>;</p> <p>(c) for each <u>Financial Year</u>, a <u>consolidated</u> cash flow statement for the <u>Relevant Group</u>;</p> <p>(d) for each <u>Financial Quarter</u>, a <u>consolidated</u> cash flow projection statement for the <u>Relevant Group</u> in respect of that <u>Financial Quarter</u> together with the five <u>Financial Quarters</u> that follow that <u>Financial Quarter</u>;</p> <p>(e) for each <u>Financial Year</u>, a <u>Strategic Business Plan</u> for the <u>Relevant Group</u>;</p>
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	<p>(f) for each <u>Financial Year</u>, an annual reconciliation of the <u>consolidated</u> income statement, a <u>consolidated</u> balance sheet statement and a <u>consolidated</u> cash flow statement for the <u>Relevant Group</u> with the <u>consolidated</u> accounts of <u>RMH plc</u>; and</p> <p>(g) for each <u>Financial Year</u>, the <u>Annual Budget</u> for the <u>Relevant Group</u>.</p>
<p>USPAC</p> <p>1.3.2</p> <p><i>Accounting standards & Pro-formas</i></p>	<p><u>Royal Mail</u> must prepare the financial statements and information required under USPAC 1.3.1 applying the accounting standards and methodologies used in the statutory <u>consolidated</u> accounts of <u>RMH plc</u>, and by using the pro-formas corresponding to the statement or information in question prescribed by <u>OFCOM</u> in the <u>Regulatory Accounting Guidelines</u> or otherwise as <u>OFCOM</u> may direct from time to time.</p>
<p>USPAC</p> <p>1.3.3</p> <p><i>Additional requirements</i></p>	<p><u>Royal Mail</u> must prepare and maintain the financial statements and information required under USPAC 1.3.1 in accordance with such additional requirements prescribed by <u>OFCOM</u> in the <u>Regulatory Accounting Guidelines</u> or otherwise as <u>OFCOM</u> may direct from time to time.</p>
<p>USPAC</p> <p>1.3.4</p> <p><i>Auditing</i></p>	<p><u>Royal Mail</u> must secure an appropriate audit opinion by a <u>Qualified Independent Auditor</u> in respect of each of the financial statements and information required under USPAC 1.3.1(a), (b), (c) and (f), on the basis directed by <u>OFCOM</u> from time to time. <u>Royal Mail</u> must include that audit opinion in the financial statement and information in question.</p>
<p>USPAC</p> <p>1.3.5</p> <p><i>Auditing</i></p>	<p><u>Royal Mail</u> must select and appoint the <u>Qualified Independent Auditor</u> for the purpose of USPAC 1.3.4. <u>Royal Mail must notify upon OFCOM in writing of the appointment of the Qualified Independent Auditor giving their approval to the appointment and the terms of the engagement, <u>60 days prior to the appointment</u>.</u></p>
<p>USPAC</p> <p>1.3.6</p> <p><i>Auditing</i></p>	<p><u>Royal Mail</u> must remunerate the <u>Qualified Independent Auditor</u> and meet the costs of the audit.</p>
<p>USPAC</p> <p>1.3.7</p> <p><i>Publication</i></p>	<p><u>Royal Mail</u> must publish each of the financial statements and information required under USPAC 1.3.1(a), (b), (c) and (f) by placing a copy of the statements and information on any relevant website operated or controlled by <u>Royal Mail</u> within 120 <u>days</u> after the end of the <u>Financial Year</u> for which the statement has been prepared.</p>
<p>USPAC</p>	<p><u>Royal Mail</u> must send a copy of a financial statement and information required to be published under USPAC 1.3.7 to any person at that person's written request. The provision of such a copy may be subject</p>

1.3.8 <i>Copy on request</i>	to a reasonable charge. For the avoidance of doubt, <u>Royal Mail</u> is not required to send any requested statement and information before the corresponding date of publication prescribed by USPAC 1.3.7.
USPAC 1.3.9 <i>Delivery to OFCOM</i>	<p><u>Royal Mail</u> must deliver to <u>OFCOM</u>—</p> <p>(a) the financial statement and information required under USPAC 1.3.1(d)—</p> <p>(i) in relation to the first <u>Financial Quarter</u> of the first <u>Financial Year</u>, by no later than 30 April 2012;</p> <p>(ii) in relation to each subsequent <u>Financial Quarter</u>, before the commencement of the <u>Financial Quarter</u> to which it relates;</p> <p>(b) the <u>Strategic Business Plan for the Relevant Group</u> financial statement and information required under USPAC 1.3.1(e) <u>and the Annual Budget for the Relevant Group required under USPAC 1.3.1(g)</u>—</p> <p>(i) in relation to the first <u>Financial Year</u>, by no later than 31 August 2012;</p> <p>(ii) in relation to each subsequent <u>Financial Year</u>, before the commencement of the <u>Financial Year</u> to which it relates;</p> <p>(ii) in relation to any subsequent update to the financial statement and information during each <u>Financial Year</u>, when the update has been approved by Royal Mail.</p> <p>(c) the financial statement and information required under USPAC 1.3.1(g)—</p> <p>(i) in relation to the first <u>Financial Year</u>, by no later than 30 April 2012; and</p> <p>(ii) in relation to each subsequent <u>Financial Year</u>, before the commencement of the <u>Financial Year</u> to which it relates.</p>

1.4. Obligations relating to the Reported Business

USPAC 1.4.1 <i>Financial statements and information</i>	<p><u>Royal Mail</u> must prepare and maintain the following—</p> <p>(a) for each <u>Financial Year</u>, an annual income statement for the <u>Reported Business</u> as a whole;</p> <p>(b) for each <u>Financial Quarter</u>, a quarterly income statement for the <u>Reported Business</u> as a whole;</p> <p>(c) for each <u>Financial Year</u>, an annual reconciliation of the income statement for the <u>Reported Business</u> as a whole in respect of the quarterly information to be provided under USPAC 1.4.1(b) with the</p>
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	<p>annual information to be provided under USPAC 1.4.1(a), together with explanatory notes where appropriate;</p> <p>(d) for each <u>Financial Year</u>, an annual reconciliation of the income statement for the <u>Reported Business</u> as a whole in respect of the annual information to be provided under USPAC 1.4.1(a) with the corresponding equivalent information for the <u>Relevant Group</u>;</p> <p>(e) for each <u>Financial Year</u>, an annual capital employed statement for the <u>Reported Business</u> as a whole;</p> <p>(f) for each <u>Financial Year</u>, an annual reconciliation of the capital employed statement for the <u>Reported Business</u> as a whole in respect of the annual information to be provided under USPAC 1.4.1(e) with the corresponding information for the <u>Relevant Group</u>;</p> <p>(g) for each <u>Financial Year</u>, an annual cash flow statement for the <u>Reported Business</u> as a whole;</p> <p>(h) for each <u>Financial Year</u>, an annual reconciliation of the cash flow statement for the <u>Reported Business</u> as a whole in respect of the annual information to be provided under USPAC 1.4.1(g) with the corresponding information for the <u>Relevant Group</u>;</p> <p>(i) for each <u>Financial Year</u>, an annual product profitability statement for the <u>Reported Business</u> as a whole for each of the products and/or services as <u>OFCOM</u> may direct from time to time;</p> <p>(j) for each <u>Financial Quarter</u>, a quarterly product profitability statement for the <u>Reported Business</u> as a whole for each of the products and/or services as <u>OFCOM</u> may direct from time to time; and</p> <p>(k) for each <u>Financial Month</u>, a revenue, cost and volume information statement for the <u>Reported Business</u> as a whole for all such products and/or services as <u>OFCOM</u> may direct from time to time.</p>
<p>USPAC</p> <p>1.4.2</p> <p><i>Pro-formas</i></p>	<p><u>Royal Mail</u> must prepare the financial statements and information required under USPAC 1.4.1 by using the pro-formas corresponding to the statement or information in question prescribed by <u>OFCOM</u> in the <u>Regulatory Accounting Guidelines</u> or otherwise as <u>OFCOM</u> may direct from time to time.</p>
<p>USPAC</p> <p>1.4.3</p> <p><i>Additional requirements</i></p>	<p><u>Royal Mail</u> must prepare and maintain the financial statements and information required under USPAC 1.4.1 in accordance with such additional requirements prescribed by <u>OFCOM</u> in the <u>Regulatory Accounting Guidelines</u> or otherwise as <u>OFCOM</u> may direct from time to time.</p>
<p>USPAC</p> <p>1.4.4</p>	<p>Except for the financial statements and information required under USPAC 1.4.1(b), (c), (j) and (k), <u>Royal Mail</u> must secure an appropriate audit opinion by a <u>Qualified Independent Auditor</u> in respect of each of the financial statements and information required under USPAC 1.4.1,</p>

<i>Auditing</i>	on the basis directed by <u>OFCOM</u> from time to time. <u>Royal Mail</u> must include that audit opinion in the financial statement and information in question.
USPAC 1.4.5 <i>Auditing</i>	<u>Royal Mail</u> must select and appoint the <u>Qualified Independent Auditor</u> for the purpose of USPAC 1.4.4. <u>Royal Mail must notify OFCOM in writing of the appointment of the Qualified Independent Auditor and the terms of the engagement, 60 days prior to the appointment upon OFCOM giving their approval to the appointment and the terms of the engagement.</u>
USPAC 1.4.6 <i>Auditing</i>	<u>Royal Mail</u> must remunerate the <u>Qualified Independent Auditor</u> and meet the costs of the audit.
USPAC 1.4.7 <i>Publication</i>	<u>Royal Mail</u> must publish each of the financial statements and information required under USPAC 1.4.1(a), (d), (e), (f), (g), (h) and (i) by placing a copy of the statements and information on any relevant website operated or controlled by <u>Royal Mail</u> within 120 <u>days</u> after the end of the <u>Financial Year</u> for which the statement and information have been prepared. For the financial statement and information referred to in USPAC 1.4.1(i), <u>Royal Mail</u> is only required to publish information relating to <u>Relay</u> , <u>PAF</u> and such <u>Access</u> products and/or services as <u>OFCOM</u> may direct from time to time in the <u>Regulatory Accounting Guidelines</u> or otherwise.
USPAC 1.4.8 <i>Copy on request</i>	<u>Royal Mail</u> must send a copy of a financial statement and information required to be published under USPAC 1.4.7 to any person at that person's written request. The provision of such a copy may be subject to a reasonable charge. For the avoidance of doubt, <u>Royal Mail</u> is not required to send any requested statement and information before the corresponding date of publication prescribed by USPAC 1.4.7.
USPAC 1.4.9 <i>Delivery to OFCOM</i>	<u>Royal Mail</u> must deliver to <u>OFCOM</u> each of the financial statements and information required under USPAC 1.4.1(b), (c), (i), (j) and (k)— (a) for the statements and information referred to in USPAC 1.4.1(b) and (j), within <u>90-60 days</u> after the end of the <u>Financial Quarter</u> for which the statement and information have been prepared; (b) for the statements and information referred to in USPAC 1.4.1(c), within 120 <u>days</u> after the end of the <u>Financial Year</u> for which the statement and information have been prepared; (c) for the statements and information referred to in USPAC 1.4.1(i) excluding the information to be published by USPAC 1.4.7, within 120 <u>days</u> after the end of the <u>Financial Year</u> for which the statement and

	<p>information have been prepared; and</p> <p>(d) for the statements and information referred to in USPAC 1.4.1(k), within 30 <u>days</u> after the end of the <u>Financial Month</u> for which the statement and information have been prepared.</p>
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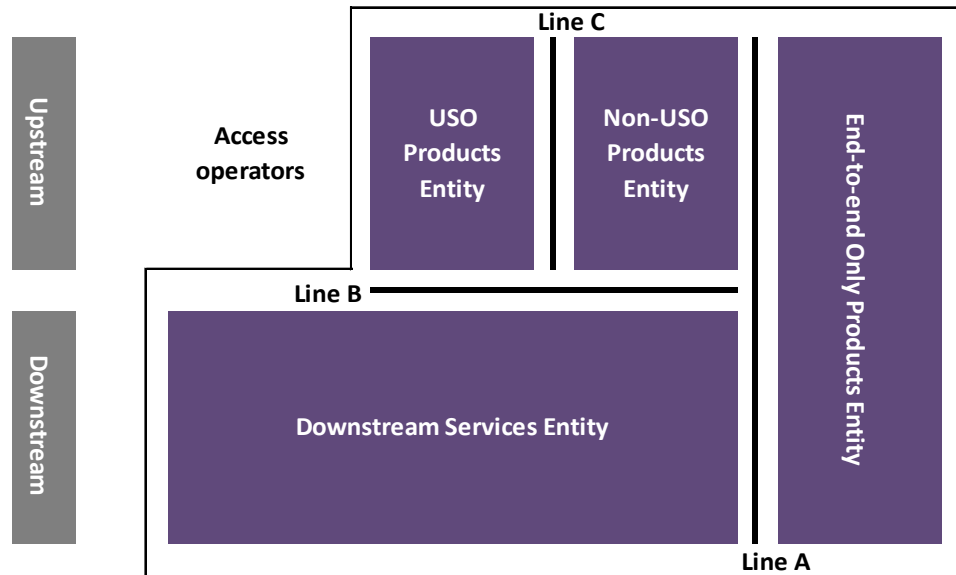
1.5. Obligations relating to the separated Reported Business

USPAC

1.5.1

Four FREs

Royal Mail must maintain a separation for accounting purposes between the activities of the four financial reporting entities (the “**Four FREs**”) within the Reported Business as represented and defined by the Lines described below—



where—

(a) **Line A** shows the separation of regulatory financial statements and information for products and/or services provided by Royal Mail in competition with products and/or services provided by postal operators, whose provision does not require the benefit of Access to Royal Mail's postal network (within the meaning of section 38(3) of the Act) to ensure effective competition and efficient provision of those products and/or services, from those that do, excluding any USO products and/or services;

(b) **Line B** shows the separation of regulatory financial statements and information for downstream services from upstream services, at the point of entry to the Inward Mail Centre, for those products and/or services whose provision require the benefit of Access to Royal Mail's postal network (within the meaning of section 38(3) of the Act) to ensure effective competition and efficient provision of those products and/or services;

(c) **Line C** shows the separation of regulatory financial statements and information for USO products and/or services within the upstream services separated by Line B, from non-USO products and/or services; and

(d) OFCOM may direct from time to time in the Regulatory Accounting Guidelines or otherwise the products and/or services which fall into each financial reporting entity.

<p>USPAC</p> <p>1.5.2</p> <p><i>Financial statements and information</i></p>	<p><u>Royal Mail</u> must prepare and maintain for each of the <u>Four FREs</u> the following—</p> <p>(a) for each <u>Financial Year</u>, an annual income statement;</p> <p>(b) for each <u>Financial Quarter</u>, a quarterly income statement;</p> <p>(c) for each <u>Financial Year</u>, an annual reconciliation of the income statement in respect of the quarterly information to be provided under USPAC 1.5.2(b) with the annual information to be provided under USPAC 1.5.2(a), together with explanatory notes where appropriate;</p> <p>(d) for each <u>Financial Year</u>, an annual end to end income statement in respect of <u>USO</u>, <u>non-USO</u> and <u>non-Mails</u>;</p> <p>(e) for each <u>Financial Quarter</u>, a quarterly end to end income statement in respect of <u>USO</u>, <u>non-USO</u> and <u>non-Mails</u>;</p> <p>(f) for each <u>Financial Year</u>, an annual capital employed statement; and</p> <p>(g) for each <u>Financial Year</u>, an annual cash flow statement.</p>
<p>USPAC</p> <p>1.5.3</p> <p><i>Pro-formas</i></p>	<p><u>Royal Mail</u> must prepare the financial statements and information required under USPAC 1.5.2 by using the pro-formas corresponding to the statement or information in question prescribed by <u>OFCOM</u> in the <u>Regulatory Accounting Guidelines</u> or otherwise as <u>OFCOM</u> may direct from time to time.</p>
<p>USPAC</p> <p>1.5.4</p> <p><i>Additional requirements</i></p>	<p><u>Royal Mail</u> must prepare and maintain the financial statements and information required under USPAC 1.5.2 in accordance with such additional requirements prescribed by <u>OFCOM</u> in the <u>Regulatory Accounting Guidelines</u> or otherwise as <u>OFCOM</u> may direct from time to time.</p>
<p>USPAC</p> <p>1.5.5</p> <p><i>Auditing</i></p>	<p><u>Royal Mail</u> must secure an appropriate audit opinion by a <u>Qualified Independent Auditor</u> in respect of each of the financial statements required under USPAC 1.5.2(a), (d), (f) and (g) on the basis directed by <u>OFCOM</u> from time to time. <u>Royal Mail</u> must include that audit opinion in the financial statement and information in question.</p>
<p>USPAC</p> <p>1.5.6</p> <p><i>Auditing</i></p>	<p><u>Royal Mail</u> must select and appoint the <u>Qualified Independent Auditor</u> for the purpose of USPAC 1.5.5. <u>Royal Mail must notify OFCOM in writing of the appointment of the Qualified Independent Auditor and the terms of the engagement, 60 days prior to the appointment upon OFCOM giving their approval to the appointment and the terms of the engagement.</u></p>
<p>USPAC</p>	<p><u>Royal Mail</u> must remunerate the <u>Qualified Independent Auditor</u> and meet the costs of the audit.</p>

1.5.7 <i>Auditing</i>	
USPAC 1.5.8 <i>Publication</i>	<p><u>Royal Mail</u> must publish each of the financial statements and information required under USPAC 1.5.2(d) by placing a copy of the statements on any relevant website operated or controlled by <u>Royal Mail</u> within 120 days after the end of the <u>Financial Year</u> for which the statement and information have been prepared. <u>Royal Mail</u> is not required to publish information prescribed as confidential by <u>OFCOM</u> in the <u>Regulatory Accounting Guidelines</u> or otherwise as <u>OFCOM</u> may direct from time to time.</p>
USPAC 1.5.9 <i>Copy on request</i>	<p><u>Royal Mail</u> must send a copy of a financial statement and information required to be published under USPAC 1.5.8 to any person at that person's written request. The provision of such a copy may be subject to a reasonable charge. For the avoidance of doubt, <u>Royal Mail</u> is not required to send any requested statement and information before the corresponding date of publication prescribed by USPAC 1.5.8.</p>
USPAC 1.5.10 <i>Delivery to OFCOM</i>	<p><u>Royal Mail</u> must deliver to <u>OFCOM</u> each of the financial statements and information required under USPAC 1.5.2(a), (b), (c), (d), (e), (f) and (g)—</p> <p>(a) for the statements and information referred to in USPAC 1.5.2(a), (c), (d), (f) and (g), within 120 days after the end of the <u>Financial Year</u> for which the statement and information have been prepared; and</p> <p>(b) for the statements and information referred to in USPAC 1.5.2(b) and (e), within 90 60 days after the end of the <u>Financial Quarter</u> for which the statement and information have been prepared in respect of the <u>Financial Quarter</u>.</p> <p>For this USPAC 1.5.10, references to the financial statements and information in USPAC 1.5.2(d) are references to any confidential information that <u>Royal Mail</u> has excluded from publication by virtue of the provision in USPAC 1.5.8.</p>

1.6. Obligations relating to the Costing Manual and the Accounting Methodology Manual

USPAC 1.6.1 <i>Costing Manual & Accounting Methodology Manual</i>	<p><u>Royal Mail</u> must prepare, maintain and keep up-to-date the <u>Costing Manual</u> for the <u>Reported Business</u> and the <u>Accounting Methodology Manual</u> in accordance with such requirements prescribed by <u>OFCOM</u> in the <u>Regulatory Accounting Guidelines</u> or otherwise as <u>OFCOM</u> may direct from time to time. Such requirements may include (but not limited to) pro-formas which <u>Royal Mail</u> must use.</p>
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<p>USPAC</p> <p>1.6.2</p> <p><i>Updates of the Manuals</i></p>	<p><u>Royal Mail</u> must prepare and maintain the following—</p> <p>(a) for each <u>Financial Quarter</u>, a quarterly update of the <u>Costing Manual</u> for the <u>Reported Business</u>; and</p> <p>(b) for each <u>Financial Quarter</u>, a quarterly update of the <u>Accounting Methodology Manual</u>.</p>
<p>USPAC</p> <p>1.6.3</p> <p><i>Notification of material changes to updates</i></p>	<p><u>Royal Mail</u> must notify <u>OFCOM</u> in writing of any material changes made to the information required under USPAC 1.6.2 <u>7 days</u> prior to the change being made. For the purpose of this obligation, a “material change” must be determined in the same manner as materiality is directed by <u>OFCOM</u> from time to time for the purpose of the <u>Regulatory Accounting Guidelines</u>.</p>
<p>USPAC</p> <p>1.6.4</p> <p><i>Auditor compliance statement</i></p>	<p><u>Royal Mail</u> must secure a statement by the <u>Qualified Independent Auditor</u> on an annual basis setting out whether or not <u>Royal Mail</u> has complied with the requirements set out in USPAC 1.6.3. <u>Royal Mail</u> must deliver to <u>OFCOM</u> that statement within <u>120 days</u> after the end of the <u>Financial Year</u>.</p>
<p>USPAC</p> <p>1.6.5</p> <p><i>Auditing</i></p>	<p><u>Royal Mail</u> must select and appoint the <u>Qualified Independent Auditor</u> for the purpose of USPAC 1.6.4 upon <u>OFCOM</u> giving its approval to the appointment and the terms of the engagement. <u>Royal Mail</u> must remunerate the <u>Qualified Independent Auditor</u> and meet the costs for that purpose.</p>
<p>USPAC</p> <p>1.6.6</p> <p><i>Publication of updates to Costing Manual</i></p>	<p><u>Royal Mail</u> must publish—</p> <p>(a) a copy of the <u>Costing Manual</u> for the <u>Reported Business</u> that complies with the requirements by or under this USPAC Condition concerning the <u>National Costing Methodology</u> only, on 1 April 2012; and</p> <p>(b) a quarterly update of the <u>Costing Manual</u> in accordance with USPAC 1.6.2(a), within 90 <u>60</u> days after the end of the <u>Financial Quarter</u> for which the update in question has been prepared in respect of the <u>Financial Quarter</u>,</p> <p>by placing a copy of the <u>Costing Manual</u> and every quarterly update of the <u>Costing Manual</u> on any relevant website operated or controlled by <u>Royal Mail</u>.</p> <p><u>Royal Mail</u> is not required to publish information prescribed as confidential by <u>OFCOM</u> in the <u>Regulatory Accounting Guidelines</u> or otherwise as <u>OFCOM</u> may direct from time to time.</p>

<p>USPAC</p> <p>1.6.7</p> <p><i>Copy on request</i></p>	<p><u>Royal Mail</u> must send a copy of the information required to be published under USPAC 1.6.6 to any person at that person's written request. The provision of such a copy may be subject to a reasonable charge. For the avoidance of doubt, <u>Royal Mail</u> is not required to send any requested information before the date of publication prescribed by USPAC 1.6.6.</p>
<p>USPAC</p> <p>1.6.8</p> <p><i>Delivery to OFCOM</i></p>	<p><u>Royal Mail</u> must deliver to <u>OFCOM</u>—</p> <p>(a) a copy of the <u>Accounting Methodology Manual</u> that complies with the requirements by or under this USPAC Condition but only to the extent that those requirements relate to USPAC 1.4.1(b), (j) and (k) and USPAC 1.5.2(b) and (c), by no later than 30 September 2012;</p> <p>(b) a quarterly update of the <u>Accounting Methodology Manual</u> in accordance with USPAC 1.6.2(b) but only to the extent required by the requirements referred to in USPAC 1.6.8(a), within 90 days after the end of the <u>Financial Quarter</u> for which the update in question has been prepared in respect of the <u>Financial Quarter</u>;</p> <p>(c) a copy of the <u>Accounting Methodology Manual</u> that complies with the requirements by or under this USPAC Condition, by no later than 31 May 2013;</p> <p>(ea) a quarterly update of the <u>Accounting Methodology Manual</u> in accordance with USPAC 1.6.2(b) that complies with the requirements by or under this USPAC Condition, within <u>90-60 days</u> after the end of the <u>Financial Quarter</u> for which the update in question has been prepared in respect of the <u>Financial Quarter</u>; and</p> <p>(eb) any confidential information in a quarterly update of the <u>Costing Manual</u> that <u>Royal Mail</u> has excluded from publication by virtue of the provision in USPAC 1.6.6, within <u>90-60 days</u> after the end of the <u>Financial Quarter</u> for which the update in question has been prepared in respect of the <u>Financial Quarter</u>.</p> <p>For the avoidance of doubt, <u>Royal Mail's</u> obligations in USPAC 1.6.8(b) shall cease to apply upon <u>Royal Mail</u> complying with its obligation in USPAC 1.6.8(c).</p>

1.7. Obligations to comply with the Guiding Principles etc.

<p>USPAC</p> <p>1.7.1</p> <p><i>The Guiding Principles etc. and their hierarchy</i></p>	<p><u>Royal Mail</u> must ensure that financial statements and information required by or under this USPAC Condition comply with the <u>Guiding Principles</u> and such other requirements as <u>OFCOM</u> may direct from time to time (including in the <u>Regulatory Accounting Guidelines</u>). Where it appears to <u>Royal Mail</u> that any of these requirements conflict with each other in a particular case, <u>Royal Mail</u> must secure that the conflict is resolved as follows—</p> <p>(a) Where the requirements of any of the <u>Guiding Principles</u> conflict with</p>
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	<p>each other, <u>Royal Mail</u> must give priority to them in the order in which they are set out in USPAC 1.7.2 (starting with compliance with the <u>Guiding Principle</u> concerning completeness, which must have the highest priority, and so on).</p> <p>(b) Subject to USPAC 1.7.1(c), where the requirements of any of the <u>Guiding Principles</u> set out in USPAC 1.7.2(a) to (g) conflict with other specific requirements as <u>OFCOM</u> may direct from time to time (including in the <u>Regulatory Accounting Guidelines</u>), <u>Royal Mail</u> must give priority to the latter specific requirements.</p> <p>(c) Where the requirement of the <u>Guiding Principle</u> in USPAC 1.7.2(h) concerning materiality conflict with other specific requirements as <u>OFCOM</u> may direct from time to time (including in the <u>Regulatory Accounting Guidelines</u>), <u>Royal Mail</u> must give priority to the former (i.e. the <u>Guiding Principle</u>). The only exception to giving such priority to the <u>Guiding Principle</u> in USPAC 1.7.2(h) is in relation to the identification of material changes for the purpose of complying with the requirements set out in USPAC 1.6.3, in respect of which <u>Royal Mail</u> must give priority to such other specific requirements as <u>OFCOM</u> may direct from time to time (including in the <u>Regulatory Accounting Guidelines</u>).</p> <p>(d) Where <u>Royal Mail</u> resolves a conflict in the manner set out above, <u>Royal Mail</u> must include in the affected financial statements and information a statement setting out the nature of the conflict and the manner in which <u>Royal Mail</u> has resolved it.</p>
<p>USPAC</p> <p>1.7.2</p> <p><i>Meaning of the Guiding Principles</i></p>	<p>The <u>Guiding Principles</u> are—</p> <p>(a) Completeness, i.e. <u>Royal Mail</u> must ensure that its <u>Regulatory Accounting Methodology</u> takes into account all the relevant revenues, costs, assets and liabilities of the business activities on which relevant financial statements and information are required by or under this USPAC Condition (including the <u>Regulatory Accounting Guidelines</u>).</p> <p>(b) Equivalence, i.e. <u>Royal Mail</u> must ensure, wherever possible, that transfer prices and/or charges for internal products and/or services (used for regulatory reporting purposes in relation to requirements by or under this USPAC Condition) are determined based on similar products and/or services provided to external parties, reflecting where appropriate the differences in the following aspects of the internal and external products and/or services—</p> <ul style="list-style-type: none"> (i) specifications of the above products and/or services; (ii) operational features of, and costs associated with, the production of the above products and/or the provision of the above services. <p>(c) Causality, i.e. <u>Royal Mail</u> must ensure, wherever possible in preparing financial statements and information required by or under this USPAC Condition, that—</p>

- (i) revenues (including revenue resulting from transfer charges);
- (ii) costs (including costs resulting from transfer charges);
- (iii) assets;
- (iv) liabilities; and
- (v) cash flows,

are attributed in accordance with the activities which cause the revenues to be earned, or costs to be incurred, or the assets to be acquired, or liabilities to be incurred, or the cash to be earned or spent.

(d) Objectivity, i.e. Royal Mail must ensure so far as is possible that each element of its Regulatory Accounting Methodology takes account of all the available financial and operational data that is relevant to that element. Where an element of its Regulatory Accounting Methodology is based on assumptions, those assumptions must be justified and supported, so far as is possible, by all available relevant empirical data. The assumptions must not be formulated in a manner which unfairly benefits Royal Mail or any other operator, or creates undue bias towards any part of Royal Mail's business or product.

(e) Accuracy, i.e. Royal Mail must ensure that its Regulatory Accounting Methodology maintains an adequate degree of accuracy, such that items included in the financial statements and information required by or under this USPAC Condition are free from material errors, including any double-counting. Materiality must be determined in accordance with the Guiding Principle in USPAC 1.7.2(h).

(f) Compliance with the statutory accounting standards, i.e. Royal Mail must ensure that its Regulatory Accounting Methodology complies with the accounting standards applied in Royal Mail's statutory accounts; with the exception of any departures as OFCOM may direct from time to time (including in the Regulatory Accounting Guidelines).

(g) Consistency, i.e. Royal Mail must ensure so far as is possible that its Regulatory Accounting Methodology is applied consistently with the Guiding Principles to the financial statements and information required by or under this USPAC Condition (including the Regulatory Accounting Guidelines). Royal Mail must ensure that any and all differences in application and/or changes from one period to another are justified by reference to the Guiding Principles.

(h) Materiality, i.e. The Guiding Principles set out in USPAC 1.7.2(a) to (h) must be applied to all material items of revenue, costs, assets, liabilities and cash flows, or material changes in those items. A material item of revenue, costs, assets, liabilities or cash flows, or a material change in those items, is one which is reasonably expected to affect the views of a competent user of Royal Mail's regulatory financial statements and information.

Table of terms defined in the Act

This table is provided for information and does not form a part of this USPAC Condition. We make no representations as to its accuracy or completeness. Please refer to the Act.

<i>Defined term</i>	<i>Section of the Act</i>
<i>designated USP condition</i>	<i>65(1)</i>
<i>OFCOM</i>	<i>90</i>
<i>postal network</i>	<i>38(3)</i>
<i>postal operator</i>	<i>65(1)</i>
<i>postal services</i>	<i>65(1)</i>
<i>universal service provider</i>	<i>65(1) and Schedule 9 paragraph 3(3)</i>
<i>universal service obligations</i>	<i>65(1)</i>